

## MEMORANDUM

TO: Planning & Economic Development Committee of City Council

FROM: Sam Powers, Economic Development Director

DATE: July 13, 2009

SUBJECT: Grove Arcade Public/Private Partnership

Included with this cover memo, please find information related to your PED Committee agenda item on the Grove Arcade, scheduled for this Wednesday at 3:30 p.m.

The information is divided into three subsections:

- 1) Background on the history and framework of the leasing and management arrangements for the Grove Arcade.
- 2) Financial Information
  - Certification of Participation (COPS) Financing
  - CDBG Loan to Grove Arcade Tenant Grove Corner Market
- 3) Information provided by the Grove Arcade on their previous and current business plan and model.

City staff and Grove Arcade representatives will attend the PED meeting to present the information and to answer questions generated during the committee discussion.

## MEMORANDUM

TO: Asheville City Council Planning and Economic Development Committee

FROM: Robert W. Oast, Jr., City Attorney

DATE: July 12, 2009

RE: Grove Arcade

This memorandum will provide the PED Committee with some historical background on the Grove Arcade project in downtown Asheville. The transactions summarized below are complex, and involve several parties and legal entities.

### **Brief History**

The Grove Arcade building, built in the 1920's and initially operated as a public market, was taken on by the U.S. Government in 1942, for the accommodation of federal offices in support of the war effort. In connection with the federal government's use of the building, the windows were bricked in, and the interior was converted to office use.

In the 1980's, the federal government relocated its Asheville offices to the new building on Patton Avenue, and the Grove Arcade building was closed. At about this time, a committee was formed to explore the possibility of returning the Grove Arcade, and returning it to its original intended use as a public market. This committee consisted of former mayors, former Council members, business and other community leaders. There were extensive discussions with federal elected representatives and government staff. A non-profit corporation, the Grove Arcade Public Market Foundation (GAPMF), was formed to facilitate these discussions.

### **City involvement/Operating-financing structure**

In 1997 the City acquired the Grove Arcade Building from the federal government by quitclaim deed. While the acquisition was essentially without consideration, the acquisition was pursuant to the National Monuments Act, and the instruments of conveyance contain significant restrictions on its use, and prescribe the manner of renovation and redevelopment. The "Program of Preservation and Utilization," which was part of the terms of the conveyance, requires rehabilitation of the Arcade building for a public market on the first floor, and a combination of residential and offices on the upper floors.

In August of 1997, the City entered into several of agreements with GAPMF, chiefly including the Lease and Operating Agreement, to carry out the renovation work on the Arcade Building and operate it once it opened. GAPMF in turn entered into an agreement with Skelton Development of Atlanta to renovate and operate the upper floors.

Conventional financing proved difficult to obtain and in 1999, following changes in the tax law, there was a change in the operating structure of the Arcade to establish two for-profit entities, Historic Grove Arcade Development (HGA, LLC) and Grove Arcade

Restoration (GAR, LLC), to take advantage of the federal tax credits. This arrangement required financial participation by a qualified New York Stock Exchange investor, and Carolina Power and Light Co., through CaroHome, LLC, became the investor member. Later, CaroHome essentially took the project over from Skelton Development. In 2002, Bank of America became involved in the project financially through its tax credit related investment operations, but CaroHome remained involved in the project financially and operationally.

Upon CaroHome's involvement in the project, detailed design and construction work began in earnest. Weaver Cook Construction was the general contractor. While the construction was well-executed, it took longer and proved more costly than anticipated. The building opened in 2002.

### **Current status**

The Grove Arcade building is now fully operational, with commercial spaces on the first floor, office space on the mezzanine and second levels, and residential on the third, fourth and fifth floors. In order to take full advantage of the tax credits, CaroHome had to remain involved in the project for 5 years. This period of time has now run, and Progress Energy of the Carolinas (PEC) which stepped into the place of CaroHome, is working with the other parties (GAPMF and the City), on the transition. The building is in good condition, but some repairs and maintenance are needed.

Minutes of City Council meetings dating back to 1997 reflect that Council has received extensive briefings on the Grove Arcade over the years, including the major reorganization in 1999. In addition, Council members have served on committees involved with setting up the initial structure, the reorganization in 1999, and with the construction process. In addition, Council members have served on the GAPMF board.

If you have any questions or need any further information, please let me know.

RWOjr:lm

Cc: Gary W. Jackson, City Manager

TO: Planning & Economic Development Committee of City Council

FROM: Ben Durant, CFO

DATE: July 13, 2009

SUBJECT: Grove Arcade Public/Private Partnership – Financial Information

### **Background**

In 1997, the City issued \$5,515,000 in taxable Certificates of Participation (1997C certificates) on behalf of outside organizations to support various economic development initiatives. Of this amount, approximately **\$2.6 million** was issued on behalf of the Grove Arcade Public Market Foundation (GAPMF) to renovate and restore the Grove Arcade building.

The financing of the Grove Arcade Renovation was and is intended to be a reimbursement-type transaction. That is, the City, having issued the 1997C certificates in its name, is responsible for payment of the debt service to the bank trustee; however, GAPMF, under a separate agreement, is responsible for fully reimbursing the City for the debt service expenses paid on its behalf. Specific terms of the financial arrangement between the City and GAPMF are provided below.

### **Financing Terms**

As previously stated, approximately \$2.6 million of the 1997C proceeds were issued on behalf of the GAPMF to renovate the Grove Arcade. As the issuer, the City is responsible for making the annual debt service payments on these certificates until the debt is retired in 2018. The annual debt service payments consist of principal and an adjustable interest component payable on the first business day of each month.

Under the terms of the *Preservation, Operation and Rehabilitation Agreement* (Preservation Agreement) dated August 25, 1997 between the City and GAPMF, payment of any debt (principal and interest) undertaken by the City on behalf of the Grove Arcade is guaranteed by GAPMF. The agreement further states that the source of revenue for such debt “*shall be the rents paid by the tenants of the upper floors of the Arcade (those floors above street level)*”. Thus, rents generated from the office space and the apartments occupying floors 2 through 5 represent the pledged security for the portion of the 1997C certificates designated for renovation of the Grove Arcade.

Based on the preceding, the City in effect loaned proceeds from the 1997C certificates to GAPMF to support the renovation and restoration of the Grove Arcade. A payment schedule was structured requiring GAPMF to repay the \$2.6 million in principal borrowed from the City, plus compounded interest (i.e. interest on the original principal *and* on the accumulated past interest) over the life of the loan. The interest component of the loan accrues monthly at an adjustable rate.

The specific repayment schedule included an initial payment of \$125,000. This payment was based on GAPMF's "ability to pay" rather than a structured combination of principal and interest. The first installment payment was made on June 1, 2000. The periodic required payment thereafter was \$125,000, increased annually at a rate of 3.5%, based on an anticipated improvement in the Grove Arcade's ability to pay over time. At the loan's maturity in 2018, a balloon payment is required that "catches up" on the unpaid principal and interest that accumulated over the life of the loan. A copy of the Grove Arcade's repayment schedule, with an estimated balloon payment, is provided in Attachment A.

### **Loan Guarantee**

In order to ensure that the rents paid of the tenants of the upper floors are the source of repayment of for the debt service the City has undertaken on behalf of the Grove Arcade, the Preservation Agreement includes the following provisions:

- 1) The City can require GAPMF to forward an amount equal to all the rent payments it receives from the upper floors within 30 days of receipt, accompanied with appropriate accounting documentation; or
- 2) The City can make arrangements for payment to be made directly to the City by the tenant.

Currently, the City is not exercising either of the two aforementioned options.

## MEMORANDUM

To: Planning & Economic Development Committee of City Council

From: Jeff Staudinger, Community Development Director

Date: July 9, 2009

Subject: Grove Corner Market Update

In January of 2006, the City of Asheville made a direct loan of \$75,000 to the Grove Corner market. At the time, the Market was at risk of default on its financing with the BB&T Bank, and CDBG funds had been pledged as a guarantee for that financing. The purpose of this loan was to enable the Grove Corner Market to immediately reduce its debt with BB&T Bank by \$75,000, resulting in significantly lower monthly payments for its remaining business financing with BB&T Bank.

The City agreed to make the loan at 0% interest, with complete deferral for 12 months followed by monthly payments of \$625 in principal payments only for 10 years until the debt was retired. These payments were to begin in February of 2007.

In August of 2007, staff corresponded with the Market because no payment or communication had been received, and the Market was in default of its loan agreement. The promissory note signed by the Market's owners stated that in default the interest rate would be 10%. The City offered to extend the term by six months, if the principal only payments started immediately. I have no file evidence that the Market responded to this offer.

Nonetheless, the City did not press on the default issue, and simply continued to bill the Market for \$625 monthly. I can find no evidence that any payments were made, and as of this month, the Market owes \$15,000 according to the original terms of the loan, and remains in default of the entire principal balance. The note is secured by inventory, equipment and cash reserves of the business, in second position to BB&T Bank.

Earlier this year, after notification of the situation the HCD Committee asked the staff to send another reminder letter to the Market owners. Before that letter was sent, the staff learned that the management of the Grove Arcade was in negotiation with the Market over its lease. The staff advised the HCD Committee that it was advisable to hold back on further contact with the Market until the lease issue had been resolved. Within the last two months the Grove Arcade management and the Market reached an agreement and the Market has moved from the Grove Arcade to a location on Haywood Street in West Asheville.

Since the matter of the lease has been resolved, the staff is now moving forward to remind the owners of the CDBD loan and its terms. I have called and emailed the owners asking for a meeting, with no response. The City's July bill to the Market was returned by the US Post Office. A delivery to the new address is being mailed.

Grove Arcade Public Market Foundation, Inc.  
Presentation to PED Committee  
July 15, 2009

- Original goals of the Grove Arcade Project first presented to the City Council
  - Become the prime engine for continuing the economic revitalization and renaissance in downtown Asheville.
  - Position itself as the premier public market on the East Coast, attracting national attention.
  - Play a crucial role in the rural development of the surrounding region.
  - Be a genuine celebration of the best that Asheville has to offer.
  - Encourage entrepreneurial development of owner-operated incubator businesses, with an emphasis on minority and first time business development.
  - Serve the surrounding residential community of primarily low-income elderly residents with needed goods and services.
  - Provide needed community services, human services and public amenities to the citizens of Asheville.
  - Take an active role in encouraging the development of an economically diverse downtown residential community.
  - Become a revenue generator for the City and County governments, through sales, business and real estate taxes.
  - Position itself as a fabulous local Market that draws on surrounding tourist assets.
  - Encourage people to come to downtown Asheville in the evening.
  - Prevent the Grove Arcade from remaining vacant once all Federal uses are relocated.
- Flaws to the original business model
  - Risk associated with targeted tenant population
  - Time necessary to reach full occupancy
  - Cost overruns resulted in additional bridge loan from Progress Energy of \$1.85 million on top of COPS.
  - Annual maintenance cost was originally projected at \$180,000 annually, currently it exceeds \$300,000
  - Original plan had 5 employees, we currently employ 2.5
- Actions taken by Foundation to remedy flaws in original plan.
  - Change in management
  - Change in tenant mix and leasing policy while trying to be sensitive to the vision of the original plan.
  - Reduction in staff
  - Seek reductions in overall maintenance costs
  - Initiated efforts to work with our partners to restructure our financing strategy while maintaining the building in its renovated state.

- Rents generated by the Arcade since completion are as follows:
 

2002	\$	23,810
2003		494,325
2004		834,853
2005		822,364
2006		929,318
2007		997,725
2008		946,439
- Options for financial sustainability
  - Restructure existing debt and re-amortizing it to fit current cash flows of the asset.
  - Negotiate some type of debt relief between the two major debt-holders that allows the current structure to continue or creates a new structure of ownership insuring the preservation and maintenance of the asset.
  - Divest the asset to a new development agency in satisfaction of the existing debt and subject to the existing lease with the City.